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MEMORANDUM FOR THE RECORD

SUBJECT : Record of Meeting with Secretary
of Defense

1. On 3 January I met with the Honorable James R. Schlesinger, Secretary of Defense, at his office in the Pentagon. The meeting had been arranged at my request to discuss Dr. Schlesinger's problems with a memo we had prepared for him on the share of defense in Soviet GNP. Also present at the meeting were [redacted] of OSR; [redacted] of OER; Lt. Gen. William Potts, Deputy Director of DIA; [redacted] of DIA; and Mr. Roger E. Shields, Deputy Assistant Secretary for Economic Affairs, ISA.

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Substantive Discussion

2. I started the discussion by asking Dr. Schlesinger the reasons for his skepticism about our estimates of the share of defense in Soviet GNP and what purposes he had in mind for using this particular economic measure. Dr. Schlesinger replied that he had no particular purpose other than the desire to understand the burden of defense in the USSR. He is concerned that our estimate is not a good measure of the share of national resources going to defense in the USSR and that it understates the burden of the Soviet defense effort compared with that of the US. He feels that while the share of defense in GNP may be relevant as a measure of burden in a market economy it is less relevant in the Soviet economy, which employs a different pricing system, has an entirely different structure from the US economy, and is designed to fulfill different objectives. He again used Soviet manpower estimates as an example, pointing out that defense absorbs about 10 percent of the non-agricultural labor force in terms of number of workers and, if qualitative factors could be taken into account, substantially more of the total national talent. The Secretary urged us to discourage use of the share of GNP as the single best indicator of the defense burden and to work on developing other measures. STAT

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As an aside, he deprecated the usefulness of GNP for general economic analysis as well and suggested that CIA develop alternative economic aggregates more relevant to present day economic issues.

3. Dr. Schlesinger also expressed concern that the coverage of US defense spending may be broader than that of our estimates of Soviet defense spending. He pointed out that US defense accounts include some investment expenditures and exclude reserve pay. He acknowledged, however, that the amount of error from this source is not likely to have a significant effect on the comparative shares of GNP devoted to defense in the US and USSR. Dr. Schlesinger believes that US accounts overstate real defense costs insofar as defense foots the bill for training and developing a large number of technical personnel, much of the benefits of which accrue to the civilian sector.

4. Dr. Schlesinger repeated an earlier theme that we have much to learn from Soviet defense industry, particularly in the area of military shipbuilding. This opinion carries over from his days at OMB, and appears to be based on the relative continuity of Soviet development and production programs compared with the US system. The Secretary also made the point that analysis of some of the Soviet equipment captured in the Middle East indicates that the quality and sophistication of Soviet weaponry has improved relative to our own.

Commitment

5. I told the Secretary that our annual review of Soviet defense spending is currently under way and that new estimates are likely to result in an increase of one to two percentage points in the share of defense in GNP. I also pointed out that we agree that the share of defense spending in GNP understates the relative impact of defense on the Soviet economy and that we have taken pains to point this out in our reporting. I suggested the share of defense in machinery output--the share in the USSR is about twice that in the US--as an alternative measure of the relative burden.

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6. I offered to prepare a report for the Secretary incorporating our new spending estimates and comparing the relative burden of defense in the two economies. We would include a thorough discussion of the important non-quantifiable differences between the burden of defense on the economies of both countries. I cautioned him, however, that such an analysis will require several months to complete. Dr. Schlesinger responded that it would be desirable to publish an unclassified version of the report.

General Observation

7. The discussion was quite academic in character and unusually relaxed. Dr. Schlesinger clearly enjoyed discussing the "burden" question with us. The other DoD attendees did not participate in the discussion. I interpret their presence at the meeting as Dr. Schlesinger's way of letting them know that he is still vitally interested in the topic of Soviet defense spending.

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Deputy Director for Intelligence

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Routing Slip

TO:

		ACTION	INFO.			ACTION	INFO.
1	DCI			11	IG		
2	DDCI			12	D/PPB		
3	DDS&T		✓	13	SAVA		
4	DDI	✓		14	ASST/DCI		
5	DDO			15	AO/DCI		
6	DDM&S			16	EX/SEC		
7	D/DCI/IC		✓	17			
8	D/ONE		✓	18			
9	GC			19			
10	LC			20			

SUSPENSE

Date

Remarks:

Most interesting - Maybe we need to develop several scales with their rationales & publish the resulting comparison in an unclassified article in Studies -

DCI/DCI

1/17/74